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NEED FOR AUDIT

A recent decision of the New York supreme court in New York county strikingly illustrates the need for audit when there is an insufficient internal check (*Ford, Bacon & Davis, Inc.* v. *Irving Trust Co. et al.*, 91 *N. Y. Law Journal* 2423, 5/18/34).

This was an action brought by a depositor against its bank to recover $81,500 for forged cheques paid by the bank. During a period of about nine months, six forged cheques aggregating $100,000 were paid by the defendant bank and charged to plaintiff's account. All of these cheques had been forged by plaintiff's assistant auditor, a trusted employee, and deposited by him in his personal bank account. This employee was discharged in August, 1932, and during the following month his forgeries were discovered. Plaintiff immediately notified the bank, but it then was ten months after plaintiff's receipt of the first bank statement which was accompanied by a cancelled forged cheque. The bank paid plaintiff the amount of one cheque, $18,500, but denied liability for the amount of the others on the ground that plaintiff had breached its duty to examine the monthly statements and cancelled cheques. The court sustained the bank's contention and directed a verdict for defendant.

As is evident from the following summary of the facts, an audit of only average quality would have saved plaintiff the amount of this loss and at a cost of perhaps less than one per cent. Plaintiff's employee, the assistant auditor who had committed the forgeries, was entrusted with the duty of checking and verifying the monthly bank statements and his work was never inspected or examined by any other person. He concealed his forgeries by making erasures and alterations in the bank statements and by destroying the cancelled forged cheques and the separate certificates issued by the bank to show the amounts of plaintiff's balance at the end of each month.

The court pointed out the depositor's duty to make a reasonably careful examination of bank statements and returned vouchers and to notify the bank, without unreasonable delay, of any errors. If a depositor by his negligence in failing to perform this duty enables a forger to repeat his fraud or deprives the bank of an opportunity to obtain restitution, the depositor is responsible for the damage caused by his default.

A LONG LITIGATION

In the *New York Law Journal*, a daily newspaper for lawyers, for May 9, 1934, appeared the laconic "Verdicts for defendants" to show the disposition of several important jury cases which had been tried together in the United States district court for the southern district of New York. The titles of the two cases which had been selected as representative of the group, all similar, were *O'Connor et al*, v. *Ludlam et al.*, and *Parmley* v. *Ludlam et al.* The trial of these cases continued for thirteen weeks, and at the conclusion the jury brought in a verdict for the defendants. A review of the testimony and the evidence presented to the jury during these thirteen weeks would manifestly be

impossible in the amount of space here available but, because of the importance of the litigation and the public interest in it, the claims made by the plaintiffs, of which all the important ones were denied by the defendants, are summarized. The following statement of plaintiffs' claims is based on allegations made in the complaint, which is a formal document stating plaintiffs' version of the transactions which plaintiffs claim imposed an obligation on defendants to reimburse plaintiffs for their losses. The complaint and defendants' answer are public records open to the inspection in the office of the clerk of the court where the cases were tried. The judge's charge to the jury and the court reporter's transcript of the testimony are not open to inspection in the clerk's office and therefore are not discussed in this brief review.

Defendants were public accountants and it was alleged that as such they prepared and certified a balance-sheet of a certain corporation which was engaged in the city of New York in acquiring, purchasing and selling stocks, bonds, notes, mortgages and other evidences of indebtedness. The balance-sheet in question was as of August 31, 1925, and it purported to show what the corporation's financial condition would be after giving effect to certain proposed new financing. The corporation included that balance-sheet or the substance of it in a prospectus advertising the sale of the corporation's 8 per cent. cumulative, participating, preferred stock. One of the plaintiffs alleged that in reliance upon that balance-sheet he purchased some of the stock. Later he found this stock to be worthless and he sued the accountants for the amount of his loss.

In the complaint there were the usual allegations, denied by defendants, that defendants' audit was negligently, carelessly and unskillfully made and that the balance-sheet was similarly prepared. More specifically, the complaint alleged that the balance-sheet did not indicate that certain cash balances and securities had been pledged; that it did not disclose that certain funds were held in trust; that it stated balances due from subsidiary and affiliated companies, mostly of no value, as secured notes and accounts receivable and accrued interest; that it stated liabilities as trustee as simple debts; that it did not disclose contingent liabilities; that it did not take into account the expense, about $200,000, which would be incurred in selling 30,000 shares for $3,000,000; that it erroneously stated the relations between past net earnings and dividend requirements; and that it failed to disclose that the corporation was accountable to customers for one and a half million dollars for bonds sold but not yet delivered.

So far as this particular litigation is concerned, the jury's verdict for the defendants is a conclusive disposition. But the cost of defending an action of this highly technical character in a jury trial of thirteen weeks duration must have been enormous. Possibly the listing of the substance of each allegation in the complaint may be of suggestive value as indicating the principal points upon which a balance-sheet of this type may be subject to attack.

PROOF OF MAILING

There is a presumption in the law that a letter properly addressed, stamped and mailed was delivered to the addressee. This presumption is only prima facie and can be rebutted or overcome, but positive, sworn testimony (not proved to be false) that a properly addressed and stamped letter was mailed

at a specified time in a specified post office or post box is difficult to overcome. Positive, sworn testimony by the addressee that such letter was never received raises a question of fact. Theoretically, a prima facie presumption so denied does not strengthen the case of the person who has the burden of proving that the letter was received, but practically the presumption of delivery is so strong that many persons are content to rely upon it and to save the time and expense required in registering letters. A practical expedient for one who desires to rely on the presumption is the use of post-office department form 3817. This form is a receipt, issued at the time of mailing in a post office, which shows the names and addresses of the sender and the addressee. The cost is a one cent stamp affixed to the form and cancelled by the post-office clerk. This constitutes the best proof of mailing and the best way of raising the presumption of delivery.